

Message Text

CONFIDENTIAL

PAGE 01 MANILA 12714 100924Z

10

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E.O. 11652: GDS

TAGS: ENRG, RP

SUBJECT: NEW PETROLEUM EXPLORATION LAW

BEGIN L.O.U.

SUMMARY. GOP HAS ISSUED NEW PETROLEUM LAW WHICH CONSOLIDATES ALL GOVERNMENT OIL RELATED ACTIVITY IN PETROLEUM BOARD, AND FORCES ALL CONCESSION HOLDERS TO FORM SERVICE CONTRACTS WITHIN ONE YEAR OR LOSE CONCESSIONS. GOP APPEARS SERIOUS IN EFFORTS TO RATIONALIZE AND STIMULATE OIL EXPLORATION. REACTION OF PRIVATE SECTOR HAS BEEN MIXED BUT GENERALLY POSITIVE. ACTIVITY NOW FOCUSED ON PETROLEUM ASSOCIATION'S REJOINDER TO IMPLEMENTING REGULATIONS BEING FORMULATED BY PETROLEUM BOARD. END SUMMARY

1. GOP ANNOUNCED LAST WEEK PRESIDENTIAL DECREE 782. THIS DECREE: (1) TRANSFERS ALL REGULATORY POWERS AND APPLICABLE APPROPRIATIONS, RECORDS, EQUIPMENT AND PROPERTY PERTAINING TO OIL EXPLORATION, DEVELOPMENT, AND PRODUCTION STILL RESIDING IN THE DEPT OF NATURAL RESOURCES TO THE PETROLEUM BOARD; (2) REQUIRES ALL HOLDERS OF PETROLEUM EXPLORATION CONCESSIONS AND PUBLISHED PETROLEUM EXPLORATION CONCES-
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PAGE 02 MANILA 12714 100924Z

SION APPLICATIONS UNDER THE PETROLEUM ACT OF 1949 TO

CONVERT THEIR CONCESSIONS TO SERVICE CONTRACTS UNDER TERMS AND PROVISIONS OF PRESIDENTIAL DECREE NO. 87 OF 1972. CONVERSION MUST BE ACCOMPLISHED WITHIN ONE YEAR OR THE CONCESSION WILL BECOME PART OF NATIONAL RESERVE AREA.

2. THE OFFICIAL REASONS GIVEN FOR THIS ACTION ARE TO RATIONALIZE THE OIL EXPLORATION INDUSTRY AND TO STIMULATE THE SEARCH FOR OIL. FEELING IS THAT THE PRIVATE SECTOR IS TOO FRAGMENTED WITH OVER 45 FIRMS HOLDING CONCESSIONS - SOME ACTIVE, MANY NOT. ALSO, IN PART, AND AS A LONG-ESTABLISHED HABIT, SOME DRILLING AND OTHER ACTIVITY HAS BEEN AIMED MORE AT THE STOCK MARKET THAN AT FINDING OIL. THE PETROLEUM BOARD LOOKS AT THEIR THREE YEAR EXPERIENCE WITH SERVICE CONTRACTS UNDER P.D. 87 AS SUCCESSFUL IN WIDENING THE SEARCH FOR OIL AND ATTRACTING FOREIGN CAPITAL. TO DATE THERE ARE 13 SERVICE CONTRACTS, 11 INCLUDING VARIOUS CONSORTIUMS INVOLVING 15 U.S. FIRMS. MOST FIRMS HAVE 2 TO 3 YEARS OF INTENSIVE SEARCH AHEAD OF THEM. IF NOT SUCCESSFUL IN THAT TIME, THE MAJOR OIL COMPANIES WILL LOSE INTEREST OR DIRECT RESOURCES TO MORE PROMISING AREAS. P.D. 782 IS DESIGNED TO CONSOLIDATE THE 60 PERCENT OF EXPLORABLE AREA PRESENTLY UNDER SCATTERED CONCESSIONS INTO LARGE ENOUGH BLOCKS TO ENTICE THE MAJORS INTO SERVICE CONTRACTS ON SHORE AS WELL AS OFF SHORE. THE PRIVATE FIRMS CAN DO THIS THEMSELVES BY MERGING AND FORMING SERVICE CONTRACTS UNDER THE GUIDELINES OF P.D. 87 WITHIN ONE YEAR, OR THE PHILIPPINE NATIONAL OIL COMPANY (PNOC) WILL DO IT WHEN THE CONCESSIONS REVERT TO NRA STATUS.

3. LOCAL FIRMS WELCOMES CONSOLIDATION UNDER THE PETROLEUM BOARD OF ALL GOP OIL RELATED ACTIVITY, BUT THERE HAS BEEN A MIXED REACTION IN THE TRADE TO THE SECOND PROVISION OF THE DECREE. THERE IS CONSENSUS, HOWEVER, THAT 782 IS HERE TO STAY, AND CONCESSIONAIRES MUST COPE WITH IT. PRESENT ACTIVITY IS FOCUSED ON DEVELOPING A COMMON INDUSTRY POSITION PAPER ON IMPLEMENTING RULES AND GUIDELINES THAT THE PETROLEUM ASSOCIATION WILL PRESENT TO THE PETROLEUM BOARD ON SEPTEMBER 15TH. THERE IS SOME DISCUSSION ON THE SPECIFICS OF WHAT THE ASSOCIATION POSITION SHOULD BE, BUT CONFIDENTIAL

CONFIDENTIAL

PAGE 03 MANILA 12714 100924Z

THE MAIN OBJECTIONS THAT WILL BE STRESSED INCLUDE: (A) THE LACK OF CONSIDERATION SO FAR GIVEN TO STOCKHOLDER EQUITY IN CONCESSION HOLDINGS MAKES THE DECREE APPEAR VERY ARBITRARY; (B) THE SHORT TIME ALLOWED (ONE YEAR) TO NEGOTIATE A SERVICE CONTRACT APPEARS TO PLACE THE PHILIPPINE COMPANIES AT THE MERCY OF THE MAJORS; (C) NO ACCOUNT IS TAKEN IN DECREE OF EXPENDITURES TO DATE BY CONCESSIONAIRES, AND THESE SHOULD BE TAKEN INTO ACCOUNT WHEN ESTABLISHING WORK REQUIREMENTS

UNDER SERVICE CONTRACTS; (D) INSUFFICIENT THOUGHT HAS BEEN GIVEN TO NEED FOR GOP TO MAKE FOREIGN EXCHANGE AVAILABLE TO PHILIPPINE COMPANIES TO PURCHASE AND/OR HIRE EXPLORATION EQUIPMENT, INSTEAD OF DEPENDING SOLELY ON FOREIGN MEMBERS OF SERVICE CONTRACTS TO PROVIDE IT.

4. WITH SOME EXCEPTIONS, THERE IS NOT MUCH FEELING THAT THIS ACTION IS A LAND GRAB ON PART OF PNOC. LOCAL COMPANIES UNDERSTAND GOP CONCERN FOR DOMESTIC OIL SUPPLIES AND SEE NEED TO MERGE OPERATIONS, MOBILIZE CONCESSIONS AND OTHERWISE STIMULATE EXPLORATION. THEY DO FEEL TERMS OF DECREE UNFAIR AND LOCAL FIRMS HAVENOT BEE GIVEN DUE CREDIT FOR EXTENT OF ACTIVITIES TO DATE. THEY ALSO FEEL THERE SHOULD HAVE BEEN PRIOR CONSULTATION BEFORE PROMULGATION OF DECREE. THESE ARE POINTS THAT WILL BE STRESSED IN NEGOTIATING IMPLEMENTING REGULATION WITH THE PETROLEUM BOARD.

5. COMMENT: THE BOARD IS NOT EXPECTED TO BE TOO RESPONSIVE TO ASSOCIATION VIEWPOINTS. THERE IS LITTLE SYMPATHY FOR STOCKHOLDER EQUITY BASED ON SPECULATIVE TRADING, AND DRILLING. OBJECTIVE IS EFFECTIVE MOBILIZATION OF LIMITED CAPITAL RESOURCES AND A MORE EFFECTIVE TARGETING OF RESOURCES ON PRIORITY AREAS OF EXPLORATION. GOP OIL OFFICIALS ARE KNOWN TO LOOK WITH FAVOR ON THE PERTAMINA (INDONESIAN) MODEL WHILE RECOGNIZING THE DIFFERENCES IN SITUATIONS, E.G. PROVEN VS. UNPROVEN TERRITORY. LOCAL FIRMS THAT ARE SERIOUS COMPANIES, WITH OIL EXPERTISE AND DEDICATION TO EXPLORATION WILL, BY BEING AGGRESSIVE IN MERGERS AND CONTRACT NEGOTIATIONS, MAINTAIN THEIR CONCES- SION RIGHTS. OTHERS WILL PROBABLY LOSE THEIRS TO NATIONAL RESERVE AREAS AND THUS TO PNOC. END L.O.U. BEGIN CONFIDENTIAL.

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PAGE 04 MANILA 12714 100924Z

6. MOST OBVIOUS EFFECT OF DECREE 782 IS TO GREATLY ENHANCE THE POWER OF PNOC AND OF PNOC, CHAIRMAN GERONDMO VELASCO. THE OLD BUREAU OF MINES, AS INEPT AND CURRUPT AS IT WAS, KEPT A MODICUM OF DISTANCE BETWEEN THE REGULATOR AND THE THING REGULATED. VELASCO NOW WEARS BOTH HATS, AND HE IS NOT ABOVE USING THE LINK TO COMPETITIVE ADVANATAGE. A DEFINITE PLUS, HOWEVER, MAY BE A PREVAILINGLY HIGHER QUALITY OF ATTENTION TO AND MANAGEMENT OF OIL EXPLORATION THAN HERETOFORE HAS BEEN GIVEN. ONE CAN ONLY WAIT AND SEE WHAT REWARDS, IF ANY, THAT IMPROVEMENT WILL YIELD FOR THE COUNTRY, VERSUS FOR WELL-IDENTIFIED GROUPS ALLIED WITH THE TRADITIONALLY OLIGARCHIC CONCESSIONAIRES. SULLIVAN

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